No. 93-489

In the Supreme Court of the United States

OCTOBER TERM, 1993

O'MELVENY & MYERS, PETITIONER

v.

FEDERAL DEPOSIT INSURANCE CORPORATION AS RECEIVER FOR AMERICAN DIVERSIFIED SAVINGS BANK, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE FEDERAL DEPOSIT INSURANCE CORPORATION

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QUESTION PRESENTED

The Federal Savings and Loan Insurance Corporation, acting as receiver for a failed federally insured savings institution, brought suit against a law firm for giving negligent legal advice to the institution before it went into receivership. The law firm seeks to defend the suit on the ground that the savings institution itself would have been barred from suit because the conduct of its wrongdoing officers (who retained the law firm) would have been imputed to it. The question presented is whether this wrongdoing is to be imputed to the receiver so as to bar it from pursuing claims against the law firm for damage caused to the bank's financial condition by the firm's professional malpractice.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

Cases—Continued: Page

Cases—Continued: Page

Cases—Continued: Page

Cases—Continued: Page

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-16a) is reported at 969 F.2d 744. The opinion of the district court (Pet. App. 17a-19a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on June 29, 1992. A petition for rehearing was denied on June 30, 1993. Pet. App. 22a. The petition for a writ of certiorari was filed on September 27, 1993, and was granted on November 29, 1993. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTES INVOLVED

The relevant provisions of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (FIRREA), as amended, are set forth in the appendix to this brief. App., *infra,* 1a-14a.

STATEMENT

1. This case comes to this Court on review of the court of appeals' decision reversing a grant of summary judgment to petitioner. In connection with the summary judgment motion, the parties entered into a joint stipulation of facts.[1] All inferences from those facts must be drawn in favor of the FDIC, the non-moving party.

The case arises out of the failure of American Diversified Savings and Loan Association (ADSB), a California-chartered, federally insured thrift instittuion. ADSB was also engaged in the acquisition, development and syndication of residential and commercial real estate. In a typical syndication, a subsidiary of ADSB would form a limited partnership, acquire one or more large real estate projects with funds provided directly or indirectly by ADSB, and then sell limited partnership units to individual investors. ADSB and its subsidiaries would derive income from these syndications in the form of interest charged on loans to the limited partnerships and in the form of various fees and commissions, charged to the limited partnerships for management, brokerage, and other services.

Ranbir Sahni served as ADSB's Chairman and Chief Executive Officer and owned 96% of its stock. Lester Day served as ADSB's President and owned the remaining 4% of the stock. During the time that the events at issue in this case occurred and for some time before, both Sahni and Day had "cooked the books" of ADSB in order to record sham profits that inflated ADSB's in-

[1] The Joint Stipulation can be found at C.A. Exc. of Rec. 127. We cite to the Stipulation by paragraph numbers.

come and to conceal its insolvency. ¶¶ 10, 11, 15, 16, 216. They also were taking over two million dollars in salaries, bonuses, and loans to firms in which they personally owned an interest. ¶¶ 36, 180, 183, 195.

In the period prior to April, 1985, Touche Ross & Co. was ADSB's auditor. By early April, 1985, Touche Ross had determined that ADSB's books improperly inflated the firm's assets and income. Touche Ross accordingly notified Sahni that corrections would have to be made. ¶¶ 41, 59, 60. On April 23, 1985, ADSB replaced Touche Ross with Arthur Young & Co. as its independent auditor, purportedly because Touche Ross's fees were too high. ¶¶ 64, 66. In early May, Touche Ross, despite having been replaced as independent auditor, nonetheless notified Sahni, the Federal Home Loan Bank Board (FHLBB), and Rogers & Wells (ADSB's attorneys at that time) that ADSB appeared to have a negative net worth. ¶ 67.

Although Arthur Young was able to complete an audited March 31, 1985, financial statement for an ADSB subsidiary, ADC Financial, it could not complete its audit of ADSB. By October, 1985, Arthur Young was reviewing whether a list of properties were being carried on ADSB's books at excessive values totalling approximately $60 million. ¶ 124. That amount was far greater than ADSB's reported net worth as of June 30, 1985, or $28 million. ¶ 126. James Miller, ADSB's chief financial officer, was aware of the existence of large accounting issues that could affect the solvency of ADSB. ¶¶ 55, 91, 122. Miller also knew that, since early 1984, ADSB's practices had begun to attract the concern of federal and state regulators. ¶ 37. In the second half of 1985, ADSB had come under increasing regulatory scrutiny from state and federal regulatory agencies, which took action designed to restrict the amount of ADSB's loans to its own subsidiaries or any other single borrower. ¶¶ 93, 164, 165, 170-175.

Among the syndications that ADSB had planned for 1985 were three called Hickory Trace, Wells Park, and Gateway Center, in all of which ADC Financial was to be the general partner. ¶¶ 104, 135, 146. Rogers & Wells was counsel to ADSB and its affiliates in connection with the Hickory Trace limited partnership, and Arthur Young was its auditor for that syndication. ¶ 105. A private placement memorandum (PPM) for the sale of limited partnership units in Hickory Trace was issued by an ADSB subsidiary on or about August 1, 1985, and was supplemented on September 1 and October 7, 1985. ¶ 106; see C.A. Exc. of Rec. 997-1660. The Hickory Trace PPM included financial statements for the limited partnership and ADC Financial. It did not, however, include a financial statement for ADSB itself. ¶ 109. In late September, Rogers & Wells advised ADSB that, since the financial health of ADSB was essential to the success of the project, the Hickory Trace offering could not close —*i.e.*, the prospective investors could not be admitted as limited partners—until the investors received audited financial statements for ADSB for the fiscal year ended June 30, 1985. ¶ 115. Since Arthur Young had been unable to complete those financial statements, the Hickory Trace investors' funds were returned to them on December 9, 1985, and the Hickory Trace offering was withdrawn. ¶ 118.

In September, 1985, ADSB retained petitioner to assist with the Wells Park and Gateway Center syndications, and it retained Coopers & Lybrand as auditors for those projects. Pet. App. 2a; C.A. Exc. of Rec. 158, 1666-1671. ADSB management did not disclose to Arthur Young, Touche Ross, Rogers & Wells, or any regulatory agency the existence of the Wells Park and Gateway Center offerings or its retention of petitioner; federal regulators did not learn of the offerings until eleven days before they were to close, on December 20, 1985, and did not learn that petitioner had been retained as counsel until after January 1, 1986. ¶ 149.

ADSB supplied petitioner with copies of the Hickory Trace PPM when petitioner was retained. ¶ 137. Petitioner prepared the PPM's for Wells Park and Gateway Center, which were issued to prospective investors on October 17 and November 15, 1985, respectively. ¶¶ 138-139, 148, 150; see C.A. Exc. of Rec. 1831-2157, 2166-2495. The PPMs "projected the image [of each of the syndications] as a well-run partnership whose general partner was experienced with similar limited partnerships that had been successful." J.A. 8, 13. They contained statements that ADC Financial's assets included a certificate of deposit with ADSB of almost $5 million and that "ADSB had informed ADC Financial that 'current regulations and circumstances would permit ADSB to provide [ADC Financial] and affiliates with funds projected to be needed by them from ADSB.' " J.A. 8, 13.

Both of the PPMs included the audited financial statement of ADC Financial as of March 31, 1985, which had been prepared by Arthur Young. Neither, however, included a financial statement for ADSB. ¶¶ 143, 160. Neither petitioner nor Coopers & Lybrand contacted Arthur Young with respect to the inclusion of the March 31, 1985, ADC financial statement, and Arthur Young was unaware that it was being included. ¶¶ 144, 161. In the course of preparing the PPMs, petitioner also did not communicate in any way with Miller (ADSB's chief financial officer), Touche Ross (ADSB's prior independent auditor), Rogers & Wells (ADSB's prior syndication counsel), or ADSB's federal or state regulators. ¶ 149.

Both the Wells Park and Gateway Center offerings closed on December 31, 1985. ¶¶ 145, 162. Prior to that time, ADSB had missed the deadline imposed by state regulators for completion of its June 30 audit, as well as two extensions of time. ¶ 169. Throughout the month of December, the state regulatory agency issued increasingly stiff restrictions on ADSB's activities.

¶¶ 170, 172. By December 20, 1985, the FHLBB had also imposed severe operating restrictions on ADSB. ¶ 175.

Finally, on February 14, 1986, the FHLBB declared that ADSB was insolvent and that ADSB had substantially dissipated its assets, in violation of legal requirements. FHLBB appointed the Federal Savings and Loan Insurance Corporation (FSLIC) as Conservator for ADSB. ¶¶ 200, 202. A financial statement for ADSB and its subsidiaries for that date showed a negative net worth of $398 million. ¶ 204. A few days later, FSLIC filed suit against Sahni and Day for, *inter alia,* breach of fiduciary duty, fraud, and (as to Sahni only) RICO violations. ¶ 206.

During 1986, FSLIC received a number of complaints from Wells Park and Gateway Center investors, who claimed that they had been misled by the PPMs they had received. Pet. App. 4a. Acting as conservator, FSLIC made a rescission offer to the investors in the two projects, all of whom accepted the offer and were repaid their investments in full. ¶¶ 211, 213-214. In accepting the rescission offer, the investors each assigned to FSLIC all claims of any nature arising from the offering. Pet. App. 4a-5a.

On June 3, 1988, FSLIC was appointed receiver for ADSB. ¶ 219. FDIC succeeded FSLIC as receiver on August 9, 1989. ¶ 221.

2. On May 12, 1989, FSLIC filed this suit against petitioner, charging that petitioner's representation of ADSB in connection with petitioner's preparation of the PPMs for the Wells Park and Gateway Center offerings had been negligent. The complaint alleged that petitioner, as "special securities counsel and special tax counsel" for the offerings, had "failed to exercise such skill, prudence and diligence" as "meets the standards of knowledge and skill of securities specialists." J.A. 17, 18. In particular, the complaint alleged that, "in the exercise of reasonable diligence," J.A. 11, 15, petitioner would have

discovered information concerning the insolvent financial condition of ADSB and its subsidiaries "as to which a reasonable person would attach importance" in deciding whether to invest in either the Wells Park or Gateway Center offerings. J.A. 10, 15. The negligence counts sought to recover damages caused to ADSB as a result of the rescinded offerings. J.A. 17, 18.

The district court granted summary judgment to petitioner, apparently reasoning that petitioner's only duty was to the investors in the rescinded offerings, whose investments had been refunded in full and who therefore had no further claim against petitioner. Pet. App. 17a-19a.

3. The court of appeals reversed. Pet. App. 1a-16a. The court's analysis proceeded in three distinct steps: (a) for purposes of summary judgment, petitioner breached a duty of care to its client, ADSB; (b) wrongdoing or knowledge of wrongdoing possessed by Sahni and Day should not be imputed to ADSB; and (c) even if such wrongdoing or knowledge were to be imputed to ADSB, it would not in any event be imputable to FDIC, which was acting as receiver "to protect the interests of third parties who were not privy to the bank's inequitable conduct." *Id.* at 14a-15a.

a. The court first rejected the district court's decision regarding petitioner's limited duty of care. Pet. App. 6a-9a. The court held that petitioner's client was ADSB. *Id.* at 8a. With respect to petitioner's duty to ADSB, the court noted that, under California law, "[p]art and parcel of effectively protecting a client, and thus discharging the attorney's duty of care, is to protect the client from the liability which may flow from promulgating a false or misleading offering to investors." *Ibid.* That duty includes the duty "to make a 'reasonable, independent investigation to detect and correct false or misleading materials.' " *Ibid.* In this case, there was evidence that such an investigation would at least have required "[petitioner] to contact Arthur Young, Touche

Ross, and Rogers & Wells prior to signing and releasing the PPMs," which it did not do. *Id.* at 9a.

b. Given the "basic duty to give proper advice to the client who is asking the public to invest in its offerings," Pet. App. 9a, the court considered petitioner's argument that, because insiders of the failed institution (Sahni and Day) perpetrated a fraud, their wrongdoing must be attributed to the institution, which would then be estopped from suing. *Id.* at 10a-13a. Citing California decisions, the court observed that a corporation is "a distinct legal entity separate from its stockholders and from its officers," *id.* at 10a, and that the question thus reduced to "whether Sahni and Day's wrongdoing as corporate *officers* can appropriately be attributed to ADSB." *Id.* at 11a. The rule of law governing that situation was that "the knowledge acquired by the agent who is acting adversely to his principal will not be attributed to the principal," *ibid.* (quoting *Meyer v. Glenmoor Homes, Inc.*, 54 Cal. Rptr. 786, 800-801 (Cal. Ct. App. 1966)).

In applying this adverse interest principle to this case, the court relied (Pet. App. 11a-12a) on a trio of cases in which federal courts had confronted the same issue: *Schacht* v. *Brown*, 711 F.2d 1343 (7th Cir.), cert. denied, 464 U.S. 1002 (1983); *Cenco Inc.* v. *Seidman & Seidman*, 686 F.2d 449 (7th Cir.) (applying Illinois law), cert. denied, 459 U.S. 880 (1982); and *In re Investors Funding Corp. Sec. Litigation*, 523 F. Supp. 533, 540-541 (S.D.N.Y. 1980) (applying New York law). The rule that emerged from those cases was that "conduct aggravating a corporation's insolvency and fraudulently prolonging its life does not benefit that corporation." Pet. App. 12a. Since "disaster, not benefit, accrued to ADSB through the malfeasance of" its officers, the court held that the insiders' wrongdoing should not be attributed to the institution under the adverse interest rule. *Ibid.* The court distinguished the key California cases cited by petitioner on the ground that they involved a liability that would have been imposed on "an

innocent third party," a status that a tortfeasor like petitioner could not claim. *Id.* at 13a n.8. To grant a tortfeasor an immunity from suit at the expense of the innocent victim of the fraud would not "serve the objectives of tort liability" of "properly compensating the victims of the wrongdoing and deterring future wrongdoing." *Id.* at 12a.

c. Finally, the court held that, even if the wrongdoing of Sahni and Day "would be imputed to ADSB so that ADSB would be estopped from bringing this lawsuit," it ought not be imputed to the FDIC as receiver. Pet. App. 13a. The court observed that "federal, not state, law governs the application of defenses against FDIC," *ibid.*, and that, to the extent that state law provides inadequate recognition of the FDIC's unique role, it ought not be incorporated into federal law. *Id.* at 13a-14a. The court noted that the FDIC as receiver "was neither a party to the original inequitable conduct nor is it in a position to take action prior to assuming the bank's assets to cure any associated defects," *id.* at 14a, and that the FDIC acts pursuant to "an intricate regulatory scheme designed to protect the interests of third parties who also were not privy to the bank's inequitable conduct," *id.* at 14a-15a. Accordingly, "imputing the bank's inequitable conduct to the receiver" in a situation like the present case would "frustrat[e]" the statutory scheme by "diminishing the value of the asset pool held by the receiver and limiting the receiver's discretion in disposing of the assets." *Id.* at 15a.

SUMMARY OF ARGUMENT

The complaint in this case alleged that petitioner failed to exercise the care commonly expected of professionals in its field, thus breaching a duty to ADSB, its client. The court of appeals applied state law in finding that the summary judgment record supported that allegation, the petition did not challenge that holding, and, in the present posture of this case, the basic allegation of malpractice must therefore be taken as true. Had petitioner committed a similar dereliction of duty in a context not involving fraud by its client's officers, petitioner would concededly be liable in damages for any injuries suffered by its client. Petitioner's basic contention is that it is nevertheless entitled to full immunity from tort liability because its negligence related to the fraudulent acts of its client's officers.

Virtually all jurisdictions, including California, generally hold a corporation liable for the knowledge of its officers, except when those officers are acting adversely to the interests of the corporation. As the court of appeals realized, the key question in this case is thus whether ADSB's officers Sahni and Day were acting for the benefit of—or adversely to—the interests of ADSB in hiding the bank's true financial condition. In our view, the court of appeals correctly decided that, because ADSB was insolvent at the time of petitioner's negligence, its fraudulent officers were necessarily acting adversely to the bank by prolonging that insolvency. As a result petitioner, which would have discovered the bank's insolvency had it acted with reasonable care, cannot now invoke the officer's wrongdoing as a defense to an action for harm caused by its own negligence.

We believe that this result follows from a sound application of generally accepted legal principles. But even if the law of a given jurisdiction were to support application of an imputation defense in the circumstances of this case, that defense nevertheless could not apply as a matter of federal common law. This case clearly arises under federal law and involves the rights of a federal agency engaged in an important nationwide program. The FDIC as receiver therefore stands in a fundamentally different position from a receiver protecting the interests of ordinary commercial creditors in a nonbanking corporation. Unlike the relationship between an ordinary commercial creditor and an ordinary corporation, the FDIC's relationship with an insured financial institution does not result from a consensual transaction, but from the application of a federal statute. Moreover, also unlike any ordinary commercial creditor, the FDIC's potential risk in insuring a given financial institution is in effect unlimited, amounting to many times the value of the stockholder's equity in the institution. Finally, the FDIC provides such insurance not for private profit, but for the public welfare and the nation's economic health. For all those reasons, the FDIC as receiver for an insolvent federally insured institution cannot be barred by insider wrongdong from recovering damages caused to an institution by a negligent law firm or accountant that had a duty to discover that insolvency.

In its brief on the merits, petitioner claims for the first time in this litigation that there is no room for a federal common law rule in this case because Congress has codified the rules applicable to professionals working for financial institutions. That contention is mistaken. In enacting recent banking legislation, Congress did modify and enlarge the FDIC's authority in a number of areas, while remaining entirely silent regarding the issues in this case. There is no basis for construing Congress's silence as an implicit directive to federal courts to stop applying federal common law to cases of this kind. It would turn the federal statute on its head to presume that, by strengthening the hand of the FDIC and other bank regulatory agencies to regulate the banking industry, Congress thereby implicitly limited the rights of the FDIC as receiver to recover for damages that insured institutions suffer at the hands of bank officers, directors, and professionals.

ARGUMENT

I. THE WRONGDOING OF ADSB'S INSIDERS DOES NOT BAR THE FDIC AS RECEIVER FROM PURSUING THIS ACTION FOR DAMAGES TO ADSB CAUSED BY PETITIONER'S NEGLIGENCE

Since the choice of federal common law depends in great part on the specific legal context, our argument that federal common law applies to this case proceeds in two steps. First, we analyze the precise issue presented by this case and the context in which recognition of a federal common law rule is sought. As we explain, the rule we believe governs this case follows from largely undisputed legal principles that do not vary widely among jurisdictions; the key precedents applying those principles to fact situations comparable to that here were relied upon by the Ninth Circuit and support its result in this case. According to those authorities, we think it clear that, where a professional retained by a federally insured financial institution commits malpractice that aggravates or prolongs the insolvency of the institution, the fact that the institution's management fraudulently tried to conceal the insolvency does not prevent the FDIC from recovering for the malpractice.

Second, we argue that this rule governs this case as a matter of uniform federal common law, even if a particular State's law might appear to be to the contrary. That is because, whatever state law may dictate for cases involving ordinary commercial entities and their creditors, the FDIC stands in a unique posture with respect to federally insured institutions.

A. The Wrongdoing Of ADSB's Insiders Would Not Be Imputed To ADSB Under Generally Accepted Common Law Principles

1. We begin with a statement of our theory of liability in this case. In the present posture of this case, it must be taken as true that, at the time petitioner participated in preparation of the Wells Park and Gateway Center private placement memoranda, a careful professional in

petitioner's position would have obtained information showing that statements in those memoranda were materially misleading. Specifically, a careful professional would have realized the necessity of contacting Touche Ross (ADSB's recently terminated independent auditor); Arthur Young (ADSB's current auditor, who had been unable to produce up-to-date ADSB financial statements and who was conspicuously given no responsibilities for the Wells Park or Gateway Center offerings); or James Miller (ADSB's chief financial officer, who was aware of ADSB's financial problems and who was working with Arthur Young to resolve the numerous problems with ADSB's audit). Perhaps most important, a careful professional would have contacted Rogers & Wells, ADSB's counsel, who was working on a contemporaneous offering that petitioner knew of and that was cancelled, and who was conspicuously not retained to work on the Wells Park and Gateway Center offerings. Had petitioner contacted those parties, it would have learned of ADSB's serious financial difficulties and of the misleading nature of the PPMs. In preparing the misleading PPMs without having taken any of those steps, petitioner "failed to exercise such skill, prudence and diligence" as "meets the standards of knowledge and skill of securities specialists," J.A. 17, 18, thus breaching a duty owed to ADSB.

Petitioner's negligence caused ADSB harm. First, had petitioner learned of ADSB's insolvency (or worse), it would have had a duty to inform ADSB's management about the facts it discovered. That in itself would perhaps have accomplished little, since Sahni and Day knew of, and were complicit in, the fraud that sought to conceal ADSB's insolvency. But petitioner, had it acted carefully, could have further advised ADSB's management of the consequences of going ahead with the offering without disclosing ADSB's true financial condition. As the court of appeals held, "[p]art and parcel of effectively protecting a client, and thus discharging the attorney's duty of care, is to protect the client from the liability which may flow

from promulgating a false or misleading offering to investors." Pet. App. 8a. Warning ADSB of this potential liability might have caused ADSB to alter its decision to go ahead with the offerings. Had it done so, it would have saved the bank from incurring the substantial losses it suffered by reason of the aborted offering.

Second, had petitioner exercised due care and discovered the facts concerning ADSB's financial condition, and had Sahni and Day nonetheless persisted in attempting to proceed with the offerings, petitioner would have been obligated to take further actions to protect its client, ADSB. Going ahead with the offering in those circumstances could only have led to legal liability and increased costs for ADSB. Accordingly, due regard for ADSB's interests would have required petitioner to withdraw, rather than assisting in the fraud that Sahni and Day were committing. Such a withdrawal would have either killed—or at least delayed—the Wells Park and Gateway Center offerings, and would have thereby saved ADSB the costs of later rescinding them.

2. In the current procedural posture of this case, therefore, petitioner would be subject to tort liability in a suit by ADSB under general state law principles governing professional malpractice cases that are not in dispute. Petitioner contends, however, that it cannot be held liable. According to petitioner, since Sahni and Day committed the fraud that concealed the insolvency petitioner failed to discover, that fraud shoud be imputed to ADSB. As petitioner claims in explaining its imputation defense, "when wrongdoing by controlling owners, directors, or officers is imputed to the corporation, the corporation cannot assert injury to a legally protectible interest in a suit against a former outside professional to the corporation." Pet. Br. 39 n.28.[2] According to petitioner, if the "wrong-

[2] See also Pet. Br. 14 ("The issues before the court of appeals were whether the wrongdoing of Sahni and Day, and their knowledge of that wrongdoing, were to be imputed to ADSB, their wholly owned corporation, and whether this defense applied to the FDIC as receiver.").

doing" of Sahni and Day were imputed to ADSB, petitioner could be held liable neither to ADSB nor to the FDIC as receiver for ADSB.

3. The court of appeals rejected petitioner's argument. In doing so, it relied in large measure upon In doing so, however, it relied in large measure upon widely accepted legal principles.[3] Thus, the court noted that "[i]t is fundamental * * * that a corporation is a distinct legal entity separate from its stockholders and from its officers." Pet. App. 10a (internal quotation marks omitted). Accordingly, although "the knowledge of a corporate officer within the scope of his employment is the knowledge of the corporation," the "knowledge acquired by the agent who is acting adversely to his principal will not be attributed to the principal." *Id.* at 11a.

Petitioner does not appear to dispute either of these general principles. See Pet. 10-11 (referring to "the

[3] It is not entirely clear to us whether the court of appeals was applying state law or federal common law to determine that the fraud of Sahni and Day may not be imputed to ADSB. On the one hand, the court relied on three non-California cases to guide its application of the general principles governing the area to the factual setting of this case. Pet. App. 11a-12a. On the other hand, despite the court's undoubted sensitivity to the choice of law issue (evidenced by its express choice of federal law in its alternative holding regarding the FDIC's special rights as receiver), it did not explicitly state that it was departing from California law with regard to this holding. To the contrary, the court cited California cases for the general legal propositions governing the area and carefully distinguished the California cases cited by petitioner. See Pet. App. 11a-13a nn.5, 7-8. The court also introduced its discussion by reference to "principles of corporate identity and agency law [that] preclude attribution, starting with the basic distinction between a corporation and its shareholders." Pet. App. 10a (citing California cases). It is our position that federal common law does govern this issue, but that the content of the federal common law rule corresponds to the rule that would independently be adopted by most jurisdictions.

nearly universal rule that the knowledge of a corporate officer is not imputed to the corporation where the agent is acting adversely to the principal"). Indeed, most of the California cases on which petitioner relies, see Pet. Br. 37-39, as well as the cases petitioner cites from other States, see Pet. Br. App. A, recite the same general principles.

4. The crux of the dispute in this case comes in applying these universal general principles—and in particular, the "adverse interest" rule—to a situation in which a *wrongdoer* is sued, not by a solvent corporation that might have profited from the misdeeds of corporate officers, but by the FDIC as receiver for injuries caused to an *insolvent* financial institution. Putting to one side the unique role of the FDIC (which we discuss at pp. 27-34, *infra*), the principal cases dealing with this issue are the three cases cited by the court of appeals —*Schacht* v. *Brown*, 711 F.2d 1343 (7th Cir.), cert. denied, 464 U.S. 1002 (1983), *Cenco Inc.* v. *Seidman & Seidman*, 686 F.2d 449 (7th Cir.), cert. denied, 459 U.S. 880 (1982), and *In re Investors Funding Corp. Sec. Litigation*, 523 F. Supp. 533, 540-541 (S.D.N.Y. 1980).

In *Cenco Inc.* v. *Seidman & Seidman*, the independent auditors of a corporation were sued by the corporation for failing to detect fraud by the top management of the corporation; no receivership or insolvency appears to have been involved. 686 F.2d at 451. The Seventh Circuit noted that "the question has never been the subject of a reported case." *Id.* at 454. Accordingly, the court applied general principles to determine the viability of the corporation's claim. The court observed that the beneficiaries of any judgment in the case would be the corporation's shareholders, who had either benefitted from the fraud or recovered on independent claims from the auditors, or who at least were responsible for electing the

officers who committed the fraud. *Id.* at 455. Because "the stockholders should not be allowed to escape all responsibility for such a fraud," *id.* at 456, the court held that their professional malpractice action could not go forward.

In *Schacht* v. *Brown*, a similar claim was brought by the liquidator of an insolvent insurance company. The insurance company's insolvency led the Seventh Circuit to distinguish *Cenco*. See 711 F.2d at 1347-1350. In *Schacht*, the only possible benefit of the fraud was "continuing [the corporation's] existence past the point of insolvency to the detriment of outside creditors and policyholders." *Id.* at 1348. That result merely "aggravated [the corporation's] insolvency" and inflicted "real damage * * * by the diminution of its assets and income." *Ibid.* The court observed that "[i]n no way can these results be described as beneficial to [the corporation]," *ibid.*; instead "the corporate body is ineluctably damaged by the deepening of its insolvency, through increased exposure to creditor liability," *id.* at 1350. Finally, the court noted that, unlike in *Cenco*, the suit would serve the purposes of "properly compensat[ing] the victims of the wrongdoing, and * * * deter[ring] future wrongdoing," *id.* at 1348, since a recovery would inure to the benefit of the corporation's policyholders and creditors, not its stockholders, who stand last in line for recovery. *Id.* at 1348-1349.

The court in *Investors Funding* similarly analyzed the "adverse interest" test in a suit brought by a bankruptcy trustee of an investment firm. 523 F. Supp. at 540-541. Applying New York law, the court rejected the argument that "prolong[ing] [the corporation's] existence several years beyond its actual insolvency" benefitted the corporation. *Id.* at 541. As the court explained, "[a] corporation is not a biological entity for which it can be presumed that any act which extends its existence is beneficial to it." *Ibid.* Accordingly, if as a result of the fraud

the corporation's "financial situation was caused to deteriorate even further," its "prolonged artificial involvency" benefitted only the managers and controlling stockholders, not the corporation itself. *Ibid.*

The rule that emerges from three cases is that the actions of a fraudulent corporate officer whose fraud has the effect of artificially prolonging the life of an insolvent corporation are necessarily adverse to the primary interests of the corporation's creditors, who had no role in the fraud but were, instead, its primary victims.[4] That result obtains even if the actions were not adverse to the interests of the shareholders before insolvency, as in *Cenco*. Thus, in *McCandless* v. *Furlaud*, 296 U.S. 140, 158-160 (1935), this Court held that "[i]t was not within the power of the shareholders [of an insolvent corporation] to legalize * * * waste [by dominant officers/shareholders] to the detriment of" the corporation's creditors. As in this case, after insolvency the officer's fraud is adverse to the corporation, and the knowledge and

[4] The proposition on which the *Cenco/Schacht/Investors Funding* rule is based is a familiar one. This Court long ago explained that a "corporation is an entity, distinct from its stockholders as from its creditors." *Hollins* v. *Brierfield Coal & Iron Co.*, 150 U.S. 371, 383 (1893). When it becomes insolvent, "the equitable interest of the stockholders in the [corporation's] property * * * places the property in a condition of trust, first, for the creditors, and then for the stockholders." *Ibid.* Accord *McDonald* v. *Williams*, 174 U.S. 397, 403-404 (1899) ("The assets of the bank while it is solvent may clearly not be impressed with a trust in favor of creditors, and yet that trust may be created by the very fact of the insolvency and the trust enforced by a receiver as the representative of all the creditors."); Ernest L. Folk, III, *et al.*, *Folk on the Delaware General Corporation Law* § 141.2.12 (3d ed. 1993) ("[F]iduciary duties to creditors arise when one is able to establish the fact of insolvency" and those "fiduciary duties arise at the moment of insolvency, rather than upon the initiation of statutory proceedings.").

wrongdoing of the officer will accordingly not be imputed to the corporation.[5]

5. Petitioner does not directly take issue with the general validity and applicability of the adverse interest rule. Nor does it appear to quarrel with the fact that, in the circumstances of this case, the interests of the fraudulent officers of ADSB were adverse to the interests of the insolvent bank and its depositors. Relying primarily on cases dealing with commercial paper and similar transactions, petitioner asserts instead that under the law of California, as well as some 42 other jurisdictions, the wrongful actions of Sahni and Day should be imputed to ADSB even if the interests of those officers were adverse to the interests of the bank.

Petitioner's authorities for this proposition, however, address issues entirely different from those presented in this case. The leading case on which petitioner relies is

[5] Petitioner cites (Pet. Br. App. A) two malpractice cases that have not followed the *Cenco/Schacht/Investors Funding* rule. In *Seidman & Seidman* v. *Gee*, 625 So. 2d 1 (Fla. Dist. Ct. App. 1992) (per curiam), a Florida intermediate appellate court erroneously imputed a fraudulent agent's knowledge to a corporation, in a case involving a suit for malpractice brought by the liquidator of an insolvent insurance company; as *Schacht* v. *Brown* makes clear, that result was incorrect. In *Stratton* v. *Sacks*, 99 B.R. 686, 694 (D. Md. 1989), aff'd, 900 F.2d 255 (4th Cir. 1990) (Table), a federal court applying Maryland law applied the doctrine of contributory negligence to bar a negligence action by the trustee of a bankrupt mortgage company against an accounting firm. The court stated that "it is not necessary * * * to determine whether the fraud of [the mortgage company's dominant shareholder] and other officers can be imputed to the corporation." 99 B.R. at 694. After the trustee failed to advance any theory of causation, see 99 B.R. at 695-696, the court did decide that, on the facts of that case, the accounting firm's negligence had failed to cause any damage. *Id.* at 696. But that conclusion provides no support for petitioner's imputation argument. Indeed, the court entirely ignored *Schacht* and *Investors Funding*, and it cited *Cenco* only in connection with its discussion of causation and other issues. See 99 B.R. at 692 n.6, 696.

McKenney v. *Ellsworth,* 132 P. 75 (Cal. 1913). In that case, an individual made a $7,500 note payable to the president of a bank, and later made a $5,000 payment on the note. The bank president endorsed the note to the bank without noting the payment on it, in connection with a fraudulent transaction he had undertaken himself. The bank's receiver subsequently sued the maker for the entire $7,500. The case turned not on whether the bank officer's interests were adverse to the bank, but on whether the bank was a holder in due course—*i.e.*, whether it had taken the note without notice of the defense of payment. The court held that it was not a holder in due course, since the bank president had full knowledge of the payment at the time the bank received it. 132 P. at 77.[6]

Virtually all of petitioner's other cases similarly involve a negotiable or similar instrument sold to a bank or other corporation by an officer who had defrauded the innocent maker. For example, of the five other California cases cited, Pet. Br. 37-38, four involved that fact pattern.[7] And of the other 38 published decisions cited

[6] The cases from this Court cited by petitioner (Pet. Br. 40) are on all fours with *McKenney*. See *Curtis, Collins & Holbrook Co.* v. *United States*, 262 U.S. 215, 224 (1923); *J.J. McCaskill Co.* v. *United States*, 216 U.S. 504, 515 (1910); *Armstrong* v. *Ashley*, 204 U.S. 272, 283 (1907). All of them imputed a fraudulent corporate official's knowledge to the corporation, where the dispute was between the corporation and an innocent third party who had no connection to the fraud. None of them involved a tort suit against a third party wrongdoer, as does this case.

[7] *Williams* v. *Hasshagen*, 137 P. 9, 12 (Cal. 1913); *State Sav. & Commercial Bank* v. *Winchester*, 145 P. 171, 172-173 (Cal. Dist. Ct. App. 1914); *Rhinock* v. *Price*, 23 P.2d 1014, 1016 (Cal. 1933). The fifth case, *West American Fin. Co.* v. *Pacific Indem. Co.*, 61 P.2d 963, 965 (Cal. Dist. Ct. App. 1936), involved a variation, where a dishonest corporate official took out a fidelity bond on behalf of the corporation for his own dishonesty; the court held that the corporation could not collect on the bond. In all of those cases, the dispute was whether an innocent third party (the obligee on the commercial obligation or the surety firm) should bear the loss created by the corporation's dishonest officer.

in petitioner's Appendix A in which the court imputed an officer's knowledge to a corporation,[8] 31 of them arose in similar commercial paper or commercial transaction contexts, involving the allocation of loss between a wholly innocent third party and a bank or other corporation whose officer committed a fraud.[9] Five of the cases arose

[8] The Appendix to petitioner's brief cites 42 published decisions, but four of them do not appear to be relevant to petitioner's argument or to any other issue in this case. See *California Consol. Mining Co.* v. *Manley*, 81 P. 50, 53 (Idaho 1905) (alter ego doctrine); *Merchants Nat'l Bank & Trust Co.* v. *H.L.C. Enters., Inc.*, 441 N.E.2d 509, 514 (Ind. Ct. App. 1982) (notice given to husband as shareholder of corporation can constitute notice given to wife, under certain circumstances); *Capital Bank & Trust Co.* v. *Broussard Paint & Wallpaper Co.*, 198 So. 2d 204, 209 (La. Ct. App. 1967) (involving primacy of mechanic's lien as against purchase money mortgage); *Yager Pontiac, Inc.* v. *Fred A. Danker & Sons, Inc.*, 343 N.Y.S.2d 209, 212 (N.Y. App. Div. 1973) (imputnig actions of agent to principal, with no issue of adverse interest), aff'd mem., 356 N.Y.S.2d 860 (N.Y. 1974).

[9] Twenty-seven of the 38 cases involved commercial paper transactions of precisely the same pattern, and raising precisely the same issue, as *McKenney*. See *Tatum* v. *Commercial Bank & Trust Co.*, 69 So. 508, 512-513 (Ala. 1915); *Matanuska Valley Bank* v. *Arnold*, 223 F.2d 778, 781 (9th Cir. 1955) (applying Alaska law); *Hughes* v. *Riggs Bank*, 239 P. 297, 298 (Ariz. 1925); *Bowen* v. *Mt. Vernon Sav. Bank*, 105 F.2d 796, 799 (D.C. Cir. 1939); *Morris* v. *Georgia Loan, Sav. & Banking Co.*, 34 S.E. 378, 383 (Ga. 1899); *First Nat'l Bank of Monmouth* v. *Dunbar*, 9 N.E. 186, 188 (Ill. 1886); *Nissen* v. *Nissen Trampoline Co.*, 39 N.W.2d 92, 96-97 (Iowa 1949); *Supreme Petroleum, Inc.* v. *Briggs*, 433 P.2d 373, 378-379 (Kan. 1967); *Megunticook Nat'l Bank* v. *Knowlton Bros.*, 135 A. 95, 97 (Me. 1926); *Tremont Trust Co.* v. *Noyes*, 141 N.E. 93, 98 (Mass. 1923); *National Turners Bldg. & Loan Ass'n* v. *Schreitmueller*, 285 N.W. 497, 499 (Mich. 1939); *Sussel Co.* v. *First Fed. Sav. & Loan Ass'n*, 238 N.W.2d 625, 628 (Minn. 1976); *First Nat'l Bank of Morristown* v. *C.W. Leeton & Bro.*, 95 So. 445, 448 (Miss. 1923); *Newco Land Co.* v. *Martin*, 213 S.W.2d 504, 511-512 (Mo. 1948); *State* v. *American State Bank of Aurora*, 187 N.W. 769, 770-771 (Neb. 1922); *Le Duc* v. *Moore*, 15 S.E. 888, 889 (N.C. 1892); *Dewey* v. *Lutz*, 462 N.W.2d 435, 443 (N.D. 1990); *First Nat'l Bank of New Bremen* v. *Burns*, 103 N.E. 93, 96 (Ohio 1913); *Wood & Co.* v. *State*, 80 P.2d 261, 264 (Okla. 1938);

in slightly different contexts, but appear to involve the same legal principles.[10] Petitioner cites only two cases that appear to present issues similar to this case, where a

Citizens' Nat'l Bank v. *Speck*, 164 A. 810, 811-812 (Pa. 1933); *Cook* v. *American Tubing & Webbing Co.*, 65 A. 641, 654-655 (R.I. 1905); *First Nat'l Bank of West Minneapolis* v. *Harvey*, 137 N.W. 365, 369 (S.D. 1912); *Mays* v. *First State Bank*, 247 S.W. 845, 846 (Tex. Comm'n App. 1923); *Evona Inv. Co.* v. *Brummitt*, 240 P. 1105, 1111 (Utah 1925); *State Bank of Pamplin* v. *Payne*, 159 S.E. 163, 165 (Va. 1931); *Knobley Mountain Orchard Co.* v. *People's Bank of Keyser*, 129 S.E. 474, 475-476 (W. Va. 1925); *American Nat'l Bank of Powell* v. *Foodbasket*, 497 P.2d 546, 547-458 (Wyo. 1972). Four additional cases involved similar issues, but the courts declined to impute knowledge in those cases either because the third party was complicit in the fraud, because the individual who committed the fraud was not an agent of the corporation at all, or because of some other factual peculiarity. See *Vail Nat'l Bank* v. *Finkelman*, 800 P.2d 1342, 1345 (Colo. Ct. App. 1990) (agent acting in individual capacity, not within scope of authority); *Saratoga Inv. Co.* v. *Kern*, 148 P. 1125, 1128 (Or. 1915) (refusing to impute knowledge because third party seeking benefit of defense may have conspired in fraud); *Milwaukee Acceptance Corp.* v. *Dore*, 168 N.W.2d 594, 598 (Wis. 1969) (party who committed fraud not agent of party seeking to enforce note); see also *Little Red River Levee Dist. No. 2* v. *Garrett*, 242 S.W. 555, 557 (Ark. 1922) (fraudulent agent worked for both parties).

[10] See *Bates* v. *Cottonwood Cove Corp.*, 441 P.2d 622, 624 (Nev. 1968) (whether corporation is liable for salaries paid to employee who falsely stated he had license required for job, where corporate official knew statement was false); *Ross Systems* v. *Linden Dari-Delite, Inc.*, 173 A.2d 258, 263 (N.J. 1961) (liability of franchisor to innocent franchisee for fraud of franchisor's representative); *Crystal Ice Co.* v. *First Colonial Corp.*, 257 S.E.2d 496, 498 (S.C. 1979) (priority contest where agent of both mortgagees fraudulently recorded later mortgage one minute earlier than purchase money mortgage); *Post* v. *Maryland Casualty Co.*, 97 P.2d 173, 176 (Wash. 1939) (liability of bond company on fidelity bond that fraudulent corporate officer acquired to insure against his own fraud). In the one case with facts somewhat analogous to this case, *Griffith Motors, Inc.* v. *Parker*, 633 S.W.2d 319, 323 (Tenn. Ct. App. 1982), the court correctly *refused* to impute the knowledge of a corporation's agent to the corporation, in a suit for malpractice brought by the corporation against its accounting firm for failing to uncover the fraud of the corporation's business manager.

defendant sought to avoid liability for *wrongful* conduct that caused harm to an *insolvent* corporation. See note 5, *supra*.

The commercial instrument cases on which petitioner relies have nothing to do with the outcome here. All of petitioner's cases involved an *innocent* third party and a corporation whose employee or agent had participated in a fraud while acting within the scope of his employment. In all of them, the party being asked to bear the loss caused by fraud is a third party (typically someone who had borrowed money from a bank) who had no duty to the corporation of any kind, who committed no tort, and whose entirely innocent conduct caused no injury to the corporation. In that setting, the courts understandably impose the risk of loss on the corporation. As the court of appeals explained, "[c]ases where innocent victims of an agent's wrongdoing sue the principal are inapposite in this context." Pet. App. 13a n.8.[11]

[11] Petitioner also briefly advances the independent argument that there can be no causation when the management of the institution was complicit in the fraud. See Pet. Br. 38-39. The primary authority on which petitioner relies for its causation argument is *Flagg* v. *Seng*, 60 P.2d 1004 (Cal. Dist. Ct. App. 1936). Just as petitioner's commercial law authorities concerning imputation have nothing to do with tort principles of causation, *Flagg* has nothing to do with petitioner's primary authorities concerning an imputation defense. In *Flagg*, the intermediate state appellate court upheld a judgment in favor of an accounting firm accused of committing malpractice against an insolvent corporation. The court strongly suggested that there had been no negligence. See 60 P.2d at 1006. But the court rested its decision on the fact that "it in no way appears that any discovery [the accounting firm] might have made would have affected the result." 60 P.2d at 1008. That is because the faulty practice "pursued by the directors [of the corporation] was followed on the advice of their attorneys, and * * * no such blame can be attached to [the accounting firm], under the circumstances here appearing, as would justify a reversal of the judgment." 60 P.2d at 1008. The fact that the accounting firm did not cause any injury on the particular facts present in *Flagg* does not suggest that petitioner caused no injury in the very different circumstances of this case. In all events, the allegations of causation here must be taken as true on a motion for summary judgment.

Indeed, the courts that discuss the rationale behind petitioner's cases make the governing principles quite clear. The question is said to be whether "one of two innocent persons [the corporation or the maker of the note] must suffer because of the fraudulent conduct of a third person [the corporate officer]. *First Nat'l Bank of Morristown* v. *C.W. Leeton & Bro.*, 95 So. 445, 448 (Miss. 1923). The courts have recognized that, in those circumstances, the "loss or suffering should fall upon the one who by his acts has clothed the third party with the power to commit the fraud." *Ibid.*[12] The fact that the third

[12] See also *Crystal Ice Co.* v. *First Colonial Corp.*, 257 S.E.2d at 498 ("agent's fraud cannot alter the effect of his knowledge to his principal *with respect to third persons who had no connection with the fraud*") (emphasis added); *Ross Systems* v. *Linden Dari-Delite*, 173 A.2d at 263 ("though the agent may have deceived the principal as well as the victim, since the principal placed the agent in the position where he had the power to perpetuate the wrong, the principal rather than the *innocent third party* should bear the loss") (emphasis added); *Post* v. *Maryland Casualty Co.*, 97 P.2d at 177 (adverse interest exception to rule of imputed knowledge "has no application where the corporation seeks to enforce the benefit of a fraud perpetrated by its officers on a third person" because "the exception * * * is not a vehicle for the consummation of fraud"); *State Bank of Pamplin* v. *Payne*, 159 S.E. at 166 ("[H]owever much at fault the defendants were in leaving their blank notes with the bank cashier, and giving him limited authority to fill in the blanks, certainly they are no more at fault than the bank was in accrediting the cashier as its trusted agent, and thereby affording him the opportunity to commit the fraud upon the defendants."); *Hughes* v. *Riggs Bank*, 239 P. at 299 ("We realize that any solution of this case must work hardship on an innocent party, but when one of two innocent persons must suffer, it is but just that the one whose agent is responsible for the act which fixes the loss should bear the burden."); *National Bank of San Mateo* v. *Whitney*, 183 P. 789, 791 (Cal. 1919) (assuming both plaintiff corporation and defendant maker of note to be "equally *innocent of wrong*," loss "resulted from the fact that the plaintiff had in its employment in a position of trust and confidence a dishonest employee") (emphasis added); *Tatum* v. *Commercial Bank & Trust Co.*, 69 So. at 512 (knowledge will be imputed "where

party is "not guilty of fraud or deceit *or wrongdoing of any kind*" is ordinarily seen as crucial to finding the corporation liable. *State* v. *American State Bank of Aurora*, 187 N.W. 769, 770 (Neb. 1922) (emphasis added). And the fact that the corporation itself has actually benefitted from the fraud is an important factor in refusing to permit it to impose a loss on the innocent third party.[13]

6. Those same principles lead to precisely the opposite conclusion here. Petitioner here is a wrongdoer, not an innocent third party to a consensual commercial transaction. The FDIC's suit against petitioner thus does not involve any attempt to impose the burden of a loss occasioned by fraud on an innocent third party to the transaction; it involves instead the imposition of liability on a negligent tortfeasor for losses caused by its lack of due care. Indeed, the innocent party in this case is not petitioner, but the insolvent ADSB and those with a primary interest in it—the FDIC and the other parties whose interests the FDIC represents. See 12 U.S.C. 1821(d)(2)(A)(i) (Supp. IV 1992). Accordingly, the

the corporation has no other agency or representative in the matter, and the party asserting the knowledge or notice on the part of the corporation *is guilty of no negligence or fault in the transaction*") (emphasis added).

[13] See, *e.g.*, *Dewey* v. *Lutz*, 462 N.W.2d at 443 (imputation of insider's knowledge to corporation in part because "the Bank benefited from the fraudulent and deceitful scheme"); *American Nat'l Bank of Powell* v. *Foodbasket*, 497 P.2d at 548 ("if the principal * * * seeks to retain the benefits of the transaction, he is charged with the agent's knowledge"); *Newco Land Co.* v. *Martin*, 213 S.W.2d at 512 (party to whom knowledge sought to be imputed "in retaining the benefits of [the fraudulent acts] ratifies them"); *Atlantic Cotton-Mills* v. *Indian Orchard Mills*, 17 N.E. 496, 502 (Mass. 1888) (where "the person to whose benefit the fraud will inure seeks after knowledge of the fraud to avail himself of that act, *and to retain the benefit of it*, he must be held to * * * be chargeable with the knowledge of it, *so far at least as relates to his right to retain the benefit so secured*") (emphasis added).

equitable principles that require the corporation to bear the loss in petitioner's commercial paper cases lead to exactly the opposite conclusion here.

As discussed below, see pp. 28-31, *infra*, state courts only rarely have the opportunity to address situations comparable to that in this case, since bankruptcy and banking insolvency cases are ordinarily litigated in federal court. But when the state courts do address the issue, they almost uniformly adopt the *Cenco/Schacht/Investors Funding* rationale and refuse, because of the adverse interest rule, to impute the wrongdoing of bank officers to an insolvent bank.

For example, petitioner cites the Minnesota Supreme Court's decision in *Sussel Co.* v. *First Fed. Sav. & Loan Ass'n*, 238 N.W.2d 625 (Minn. 1976), which stated the general imputation principles applicable to a solvent partnership. But the Minnesota Supreme Court later decided *Bonhiver* v. *Graff*, 248 N.W.2d 291 (Minn. 1976), in which a state receiver for an insolvent insurance company sued the company's former accountant for malpractice in failing to uncover a fraud committed by corporate insiders. In response to a claim exactly parallel to that advanced by petitioner in this case, the court held that:

> [w]hether or not the company would be precluded from bringing this suit (the company was the victim of the fraud, and not the perpetrator), '[t]he receiver represents the rights of creditors and is not bound by the fraudulent acts of a former officer of the corporation.'

Id. at 296. Similarly, petitioner cites *Yager Pontiac, Inc.* v. *Fred A. Danker & Sons, Inc.*, 343 N.Y.S.2d 209 (N.Y. App. Div. 1973), aff'd mem., 356 N.Y.S.2d 860 (N.Y. 1974), for the application of the adverse interest test under New York law. But the federal district court in *Investors Funding* later applied New York law in the context of a corporation whose insolvency was artificially

prolonged by insiders' fraud to hold that the insiders' knowledge would *not* be attributed to the corporation.[14]

B. Principles Of Federal Common Law Bar Imputation Of The Wrongdoing Of ADSB's Insiders To The FDIC As Receiver

As we have explained above, the court of appeals' holding that the costs occasioned by petitioner's negligence should not be borne by the innocent depositors and other creditors of ADSB represents a sound application of generally accepted legal principles. In addition, those same legal principles constitute governing rules of federal common law that are applicable when FDIC acts as receiver for an insolvent depository instittuion that it has insured.[15]

[14] In addition, compare *Bates* v. *Cottonwood Cove Corp.*, 441 P.2d at 624 (cited by petitioner for the application of the adverse interest test in Nevada) with *Henderson* v. *Buchanan*, 52 B.R. 743, 772 (Bankr. D. Nev. 1985) (holding under Nevada law that trustee of insolvent corporaiton is not estopped from recovering for breach of fiduciary duty of corporation's directors even if corporation itself would be), judgment as to other claims rev'd in part, 131 insolvent corporation is not estopped from recovering for breach B.R. 859 (D. Nev. 1990), bankruptcy court judgment as to those claims affirmed, 985 F.2d 1021 (9th Cir. 1993); and compare *Saratoga Inv. Co.* v. *Kern*, 148 P. at 1128 (cited by petitioner for the application of the adverse interest test in Oregon) with *American Timber & Trading Co.* v. *Niedermeyer*, 558 P.2d 1211, 1221 (Or. 1976) (holding that equitable defenses good against majority stockholder/participant in wrongdoing not available against liquidator of insolvent corporation).

[15] Petitioner objects (Pet. Br. 36) to what it characterizes as FDIC's effort to "mix and match" a state cause of action with a federal rule of decision applicable to the imputation issue. Such "mixing and matching" is inevitable, of course, because federal common law frequently adopts state rules of decision. There is no presumption, however, that the use of a state cause of action requiries that state law apply to all elements of the case. In *Boyle* v. *United Technologies Corp.*, 487 U.S. 500, 512 (1988), for instance, the Court applied federal common law to supply a defense to a cause of action otherwise governed by state law, explaining

1. In *United States* v. *Kimbell Foods, Inc.*, 440 U.S. 715, 726 (1979), this Court held that "federal law governs questions involving the rights of the United States arising under nationwide federal programs." Accord *Kamen* v. *Kemper Fin. Servs.*, 111 S. Ct. 1711, 1717 (1991). This case arises under such a program, and petitioner does not argue to the contrary. As the Court explained in *Kimbell*, however, "[c]ontroversies directly affecting the operations of federal programs, although governed by federal law, do not inevitably require resort to uniform federal rules." 440 U.S. at 727-728. The Court outlined three considerations in determining "[w]hether to adopt state law or to fashion a nationwide federal rule." *Id.* at 728. First, "federal programs that by their nature are and must be uniform in character throughout the Nation necessitate formulation of controlling federal rules." *Ibid.* (internal quotation marks omitted). See, *e.g.*, *Clearfield Trust Co.* v. *United States*, 318 U.S. 363, 366-367 (1943). Second, "[a]part from considerations of uniformity," a court should "fashion special [federal] rules" where "application of state law would frustrate specific objectives of the federal programs." 440 U.S. at 728. Finally, the decision whether to fashion a federal rule should also take into account "the extent to which application of a federal rule would disrupt commercial relationships predicated on state law." *Id.* at 729.

2. Because state courts rarely or never have the opportunity to address the distinctly federal interests at stake in cases like this, there is a substantial need for a uniform federal rule. As petitioner's cases make clear, the principles underlying the state law imputation defense

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that it is frequently the case that "the conflict [between state law and federal objectives] is more narrow, and only particular elements of state law are superseded." *Id.* at 508 (citing *United States* v. *Little Lake Misere Land Co.*, 412 U.S. 580, 595 (1973), and *Howard* v. *Lyons*, 360 U.S. 593, 597 (1959)). See also *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942); *Deitrick* v. *Greaney*, 309 U.S. 190 (1940).

have largely been developed by state courts in the course of ordinary commercial litigation involving commercial paper and similar instruments and solvent financial institutions and entities. It is reasonable for a federal court to presume that those rules fully take into account the various interests at stake in that type of litigation. Accordingly, as this Court noted in *Kamen* v. *Kemper Fin. Servs., Inc.*, especially where "private parties have entered legal relationships with the expectation that their rights and obligations would be governed by state-law standards," there is thus a "presumption that state law should be incorporated into federal common law." 111 S. Ct. at 1717.

In this case, however, state law necessarily provides a perilous guide. State courts—which have limited opportunity to adjudicate cases involving insolvency in any event—very rarely have the opportunity to consider the unique considerations applicable to suits brought by the FDIC acting as receiver for insolvent financial institutions. See 12 U.S.C. 1819(b)(2)(B) (Supp. IV 1992) (FDIC's right to remove state court suits to federal court).

Unlike an ordinary commercial creditor, the FDIC does not become a creditor of a depository institution as a result of a consensual transaction. An ordinary commercial enterprise determines whether or not to extend credit to a customer and, if so, how much credit to extend, based upon an assessment of the customer's creditworthiness, including, where desirable, a judgment about the integrity of the customer's management. By contrast, federal statutes and regulations dictate the FDIC's choice of "customers," the amount of insurance it will underwrite, and the terms on which it will issue that insurance. See 12 U.S.C. 1814-1818, 1821(a) (1988 & Supp. IV 1992); see also 12 C.F.R. Pts. 303, 307, 312, 330.[16]

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[16] Although FDIC retains very substantial power to regulate insured institutions and to determine whether to insure an institu-

Unlike an ordinary commercial creditor, the FDIC's financial exposure with respect to a given institution is also effectively both unlimited and much greater than the exposure of the stockholders of the institution.[17] Under present federal standards, an insured thrift must maintain its capital at a level of approximately 5% of its assets, most of which are derived from deposited funds.[18] By contrast, the FDIC insures most of the deposits of the institution up to a level of $100,000 per account. Even with respect to an institution that fully satisfies regulatory capital requirements the FDIC's exposure to loss may therefore be twenty times that of the institution's stockholders. That level of exposure is much greater than the level that would be acceptable to an ordinary commercial creditor. As events in recent years have demonstrated, the risks underwritten by the FDIC, and through the FDIC by the taxpayers of the United States, are all too likely to materialize.

Finally, unlike ordinary commercial creditors, the FDIC insures deposits in order to stabilize and maintain public confidence in the nation's banking system—a goal that is of crucial importance to the welfare of the general public and the health of the national economy. Indeed, among

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tion, the fact remains that the decision whether to insure deposits at an institution is not a free-market, consensual transaction; FDIC must exercise its authority in strict accordance with the statutory and regultaory provisions cited in the text.

[17] The FDIC is authorized to borrow up to $30 billion from the United States Treasury "to be used by the [FDIC] solely in carrying out its functions with respect to [deposit] insurance." 12 U.S.C. 1824(a) (Supp. IV 1992). Moreover, the full faith and credit of the United States stands behind borrowing by the FDIC that meets certain statutory conditions. 12 U.S.C. 1825(d) (Supp. IV 1992).

[18] Various capital requirements for thrifts are set forth at 12 U.S.C. 1464(t) (Supp. IV 1992) and regulations promulgated in accordance iwth that statute. See also 12 U.S.C. 1831*o*(c)(3)(B) (Supp. IV 1992) (authority for federal banking agencies to set capital requirements); 12 C.F.R. 325.3 (FDIC capital requirements for insured banks).

the prime beneficiaries of the vast federal financial investment in the deposit insurance program are the insured financial institutions themselves and those—like petitioner—whose business is based in part on fees collected from them.

All of these facts put the FDIC in a quite different position from that of ordinary commercial creditors. They suggest that an imputation/estoppel defense that might be applicable to an ordinary commercial creditor ought not apply to the FDIC. Indeed, that is the lesson of *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942), which held that a side agreement that might, in ordinary circumstances, provide a perfectly proper defense to a bank's effort to collect on a note does not provide a defense when the FDIC attempts to collect on the same note after the bank has gone into receivership. See also *Deitrick* v. *Greaney*, 309 U.S. 190, 197-199 (1940) (holding that equitable estoppel defense based on fraud of bank stockholder is not applicable to the FDIC as receiver). Since the FDIC litigates virtually all of its significant cases in federal court, the States have not had the opportunity to take these situations into account in fashioning their imputation rules.

Whether an imputation defense in cases of this sort should apply thus depends on the effect of two circumstances—insolvency and the special role of the FDIC—that state courts rarely have the opportunity to address. Requiring federal courts to attempt to divine the hypothetical answers to questions that state tribunals rarely or never have the change to address would be unwise.[19] In such circumstances, there is a substantial need for a uniform federal rule of law.

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[19] The decisions demonstrate how tenuous the distinction between state and federal law is in this area. Indeed, the key decisions—as in this case—do not rely heavily on state sources, even when they are faithfully attempting to apply state law. See, *e.g.*, *Cenco*, 686 F.2d at 454 ("On this question, the Illinois cases on auditors' liability provide no guidance."); ***Investors Funding***, 523 F. Supp. at 540-541 (citing state sources for "controlling legal

3. Application of a rule of law giving the negligent professional tortfeasor a defense against the FDIC as receiver would also be inappropriate because this Court has long recognized that the rights of the FDIC as receiver for insolvent financial institutions implicate an area of "uniquely federal interests," *Boyle* v. *United Technologies Corp.*, 487 U.S. 500, 504 (1988) (citing *D'Oench, Duhme & Co.*, 315 U.S. at 457-458), where application of state law would frustrate the specific objectives of an important federal program. Applying state law rules that might not take into account the FDIC's special role in the nation's financial system could have that effect in circumstances like those in this case. If that occurred, there would be a risk of seriously injuring the federal deposit insurance system by depleting the deposit insurance fund and thus imposing the costs of professional malpractice on the nation's taxpayers, rather than on the negligent wrongdoer.

In addition, applying an imputation defense to insulate a law firm or other professional from liability for its own negligence would disserve the federal program by creating an incentive *against* diligent service to those thrift institutions that need it the most. Under petitioner's theory, a law or accounting firm working for a financially sound thrift whose insiders are not committing frauds would be fully liable for any malpractice it might commit. But if the financial institution's insiders were defrauding the institution, the attorney's or accountant's malpractice would be legally excused, even if—as here—that malpractice undoubtedly caused injury to the institution, its depositors and creditors, and the FDIC. On the other hand, if an attorney or accountant were to confront officers or directors with suspicions of wrongdoing or were otherwise to perform its duties to the institution aggressively,

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principles"—the adverse interest test—but not for application of those principles to tort suit by insolvent corporation); *Seidman & Seidman* v. *Gee*, 625 So. 2d at 2-3 (applying Florida law, but relying almost exclusively on *Cenco*).

it would risk being replaced by another firm. Indeed, that appears to have occurred in this case, when ADSB replaced Touche Ross with Arthur Young, and—more strikingly—when ADSB replaced Rogers & Wells with petitioner as counsel for its syndications.

To be sure, even under petitioner's theory, an intentional failure by a law or accounting firm to perform up to standards in an insolvency situation caused or aggravated by fraud might make the firm liable for complicity in the fraud, but such intentional malfeasance is extremely difficult to prove. The result would be that an attorney or accountant would have a perverse incentive to perform poorly at precisely the point where the institution itself, its creditors, and the FDIC have the greatest need for careful work. If professionals can contribute through their negligence to the insolvency of the institutions they serve, and then avoid liability on the ground that wrongdoing insiders were corrupt, the federal goals of promoting the stability and integrity of financial institutions will be frustrated. As the nation has seen in the case of the thrift industry, that can lead to catastrophic results. See *Lincoln Sav. & Loan Ass'n* v. *Wall*, 743 F. Supp. 901, 920-921 (D.D.C. 1990).

4. Finally, contrary to petitioner's contentions (Pet. Br. 46-48), application of a federal rule that refuses to apply the imputation defense in the circumstances of this case will have no effect at all on reasonable commercial or professional expectations. As we have shown above, the authority in support of petitioner's claim that California—or other States—would apply an imputation defense in the circumstances of this case is extremely weak; on the contrary, the leading cases in the area support the court of appeals' result. There is no reason to believe that any responsible law firm would enter into a representation agreement—or that any insurance company would provide it with malpractice insurance—on the premise that, should malpractice occur, liability would be in accordance

with state court decisions regarding holders in due course of commercial paper.

Moreover, even in the unlikely event that the law of California and other jurisdictions might shield petitioner from liability for its negligence based on the fraud of ADSB's insiders, that would still provide no support for petitioner's reliance argument. Any law firm attempting to determine how to represent a client properly must assume that it will be held fully liable for negligent performance of its state-law duty not to commit malpractice. Although it is possible that the firm might commit malpractice but be saved because an insider's fraud has shielded it from liability, no responsible law firm or malpractice insuror could reasonably premise their conduct or commercial arrangements on the possibility of such a windfall defense.

Finally, even if it were to be assumed that state law would provide a defense in the circumstances of this case, and even if a law firm might in some way reasonably rely on that defense in planning its representation of its clients, petitioner's argument would still have little force. It certainly would come as no surprise to professionals in the field that federally insured financial institutions can become insolvent; that a federal agency usually is appointed receiver for such an insolvent institution; and that the presence of the FDIC as receiver may alter the rights and obligations that might otherwise apply under state law. See, *e.g.*, *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942); *Langley* v. *FDIC*, 484 U.S. 86 (1987). A law firm that nonetheless entered into a representation agreement with a federally insured financial institution on the premise that federal law could not possibly apply if the institution went into receivership would be basing its conduct on wishful thinking, not reasonable commercial or professional judgment.

II. NOTHING IN FIRREA SUGGESTS THAT CONGRESS INTENDED STATE LAW TO GOVERN APPLICATION OF THE IMPUTATION DEFENSE IN THIS CASE

In its brief on the merits before this Court, petitioner principally argues (Pet. Br. 17-31) that Congress "left no room for judicial creation of a federal rule of decision to govern the tort claims of the FDIC as the receiver of a failed thrift" when it enacted FIRREA. Pet. Br. 31. Petitioner has not previously advanced that argument in any filing in this litigation.[20] Petitioner's argument is, in all events, supported neither by the case law on which it relies nor by anything in the text or history of FIRREA.[21]

1. Petitioner does not and cannot claim that Congress intended in FIRREA to "cover the field" of—and entirely eliminate—professional malpractice suits by the FDIC as receiver for insolvent financial institutions. According to petitioner, even after FIRREA such suits may be brought, so long as they are litigated entirely under state law. See Pet. Br. 24-26, 31. Thus, in order for petitioner to prevail on its new-found argument, it must demonstrate that, by enacting FIRREA, Congress intended completely to displace any federal common law governing malpractice actions by the FDIC, but nevertheless to leave state law governing such suits entirely intact. Petitioner's burden on that point is substantial; as this Court recently recognized in speaking of a federal common law doctrine

[20] Petitioner charges (Pet. Br. 19) that the court of appeals "ignored" FIRREA. In fact, the Court expressly referred to provisions of FIRREA other than those now cited by petitioner. See Pet. App. 2a n.2. Had petitioner brought the provisions of FIRREA it believes significant to the attention of the court of appeals, the court would have been more likely to address them.

[21] FIRREA was enacted on August 9, 1989. This suit, which was commenced on May 12, 1989, arose from events that occurred in 1985. We assume for purposes of this argument (as, apparently, does petitioner) that FIRREA would have taken effect in time to be relevant to this case.

alleged to have been superseded by statute, "[i]n order to abrogate a common law principle, the statute must 'speak directly' to the question addressed by the common law." *United States* v. *Texas,* 113 S. Ct. 1631, 1634 (1993).

2. Of the three primary cases cited by petitioner (see Pet. Br. 17-19) in support of its novel argument, two did not reach the conclusion that a federal statute displaced federal common law, while leaving state law fully intact. Those two cases are therefore entirely inapposite.

a. In *Northwest Airlines, Inc.* v. *Transport Workers Union,* 451 U.S. 77, 95 n.34 (1981), this Court refused to imply a federal common law right of contribution in favor of a defendant who violated the Equal Pay Act and Title VII and against a union that bore partial responsibility for those statutory violations. The Court relied on the facts that "[t]he liability of [the defendant] for discriminating against its female cabin attendants is entirely a creature of federal statute," and that those federal statutes constituted "a comprehensive legislative scheme including an integrated system of procedures for enforcement." 451 U.S. at 97. Neither of those factors is present here. More important, however, the Court concluded that it would not upset the legislative balance by adding a new common law remedy of contribution to the "comprehensive" federal statutory scheme creating the cause of action; it did not even suggest that state law would be available to supply any such right. To the contrary, the Court expressly held that cases recognizing "a right to contribution under state law in cases in which state law supplied the appropriate rule of decision" were "inapposite." *Id.* at 97 n.38.

b. In *Langley* v. *FDIC,* 484 U.S. 86 (1987), the Court held that, under 12 U.S.C. 1823(e), borrowers on a note could not rely on an unwritten side agreement to defend against an action on the note by the FDIC. Petitioner asserts (Pet. Br. 18-19) that, because the side agreement would have violated the common law doctrine of *D'Oench, Duhme,* and because the Court relied on the statute rather than that common law doctrine to decide the case, *Langley* stands for the proposition that federal common law no longer governs the assertion of equitable defenses against the FDIC.

In *Langley,* this Court certainly decided to apply the statute, rather than the common law *D'Oench, Duhme* doctrine, to bar the defense asserted by the borrower. There is nothing in the decision, however, to suggest that the Court *sub silentio* held that the statute provided the *sole* standard to govern the validity of side agreements asserted against the FDIC. To the contrary, the Court relied on *D'Oench, Duhme* to interpret the statute. See 484 U.S. at 92-93. And the federal courts of appeals, both before and after *Langley,* have uniformly concluded that a side agreement must comport *both* with Section 1823(e) *and* with the common law *D'Oench, Duhme* doctrine in order to be valid as against the FDIC.[22] Cf. *United*

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[22] See, *e.g., FDIC* v. *Wright,* 942 F.2d 1089 (7th Cir. 1991) (FIRREA did not displace D'Oench doctrine), cert. denied, 112 S. Ct. 1937 (1992); *FSLIC* v. *Griffin,* 935 F.2d 691, 698 (5th Cir. 1991) (Section 1823(e) does not preclude application of *D'Oench, Duhme*), cert. denied, 112 S. Ct. 1163 (1992); *FDIC* v. *Kasal,* 913 F.2d 487, 491 (8th Cir. 1990) (applying both Section 1823(e) and *D'Oench, Duhme*), cert. denied, 498 U.S. 1119 (1991); *Hall* v. *FDIC,* 920 F.2d 334, 339 (6th Cir. 1990) (rejecting contention that "the common law doctrine of *D'Oench* is limited by the terms of § 1823(e)"), cert. denied, 111 S. Ct. 2852 (1991); *FSLIC* v. *Murray,* 853 F.2d 1251, 1254 (5th Cir. 1988) (holding that *D'Oench* doctrine applies to FSLIC); *Taylor Trust* v. *Security Trust Fed. Sav. & Loan Ass'n,* 844 F.2d 337, 342 (6th Cir. 1988) (same); *FDIC* v. *McClanahan,* 795 F.2d 512, 514 n.1 (5th Cir. 1986) (noting that the "discussion of [Section 1823(e)] in the legislative history does not mention *D'Oench, Duhme* * * * and there is no reason to suppose that Congress intended to forbid the rule of estoppel from being applied"); *FDIC v. de Jesus Velez,* 678 F.2d 371, 375-376 (1st Cir. 1982) (applying both Section 1823(e) and *D'Oench, Duhme*); cf. *FDIC* v. *Wood,* 758 F.2d 156, 159 (5th Cir.) (holding

States v. *Texas,* 113 S. Ct. 1631. Moreover, contrary to petitioner's suggestion, the Court in *Langley* did *not* "ma[k]e plain that it would not protect asserted federal interests that were not protected by the language of the statute." Pet. Br. 18. The Court simply "made plain" that the statute did not invalidate certain defenses not asserted in *Langley*—such as "fraud in the factum." 484 U.S. at 93-94. In doing so, the Court had no occasion to consider whether such defenses would have been invalidated by an application of the *D'Oench, Duhme* doctrine and whether, if so, they would nonetheless be valid as against the FDIC.

Finally, even if petitioner's improbable argument were accepted that the Court determined *sub silentio* in *Langley* that Section 1823(e) supplants, rather than supplements, the *D'Oench, Duhme* doctrine, it would do no good for petitioner here. Although they cover a variety of other situations, both Section 1823(e) and *D'Oench, Duhme* address the question of whether a secret side agreement may constitute a defense to an action on a note by FDIC as receiver for an insured financial institution. None of the provisions of FIRREA cited by petitioner similarly specifically address the availability of an imputation defense in a malpractice action brought by the FDIC. It is a remarkable feat of statutory construction to conclude that FIRREA nevertheless codified the law pertaining to the availability of that defense.

3. Petitioner also cites *City of Milwaukee* v. *Illinois,* 451 U.S. 304, 314 (1981). In that case, the Court held that Congress's intent in enacting the Federal Water Pollution Control Act Amendments of 1972 (the 1972 Amendments), Pub. L. No. 92-500, 86 Stat. 816, "was clearly to establish an all-encompassing program of water pollution regulation," 451 U.S. at 318, which left no

federal common law holder in due course doctrine applicable, notwithstanding Section 1823(e)), cert. denied, 474 U.S. 944 (1985).

further "room for courts to attempt to improve on that program with federal common law," *id.* at 319. The Court also suggested that state common law may still continue to operate to a limited extent in support of the purposes of the 1972 Amendments in areas not otherwise preempted. 451 U.S. at 312-313, 323-324, 327-328. But the conclusion in that case that Congress intended to displace federal common law and leave some state law intact in enacting the 1972 Amendments provides no support for a similar conclusion with respect to FIRREA.

As the Court in *City of Milwaukee* painstakingly describes, Congress intended the 1972 Amendments to create "a comprehensive program for controlling and abating water pollution." 451 U.S. at 319.[23] The 1972 Amendments established "a new system of regulation" that made it illegal for anyone to discharge pollution without a permit. *Id.* at 310-311. The permits were to be "issued either by the [Environmental Protection Agency] or a qualifying state agency." *Id.* at 311. The 1972 Amendments carefully specified the circumstances under which permits could be issued and the requirements that had to be included in permits, but also expressly reserved to the States authority to set more stringent limitations. See *id.* at 327-328. And the 1972 Amendments established a comprehensive enforcement system, allocating specific roles to the EPA, state agencies, and suits brought by public agencies and private citizens. See generally *Gwaltney of Smithfield, Ltd.* v. *Chesapeake Bay Foundation, Inc.*, 484 U.S. 49 (1987).

None of the features that led to the Court's decision in *City of Milwaukee* are present in this case. The specific problem that Illinois sought to remedy in that

[23] The Court noted that "[n]o Congressman's remarks on the legislation were complete without reference to the 'comprehensive' nature of the [1972 Amendments]." 451 U.S. at 318. It found that the 1972 Amendments were designed "to establish a *comprehensive* long-range policy for the elimination of water pollution." *Ibid.*

case—the discharge of pollutants into navigable waters—had been specifically and exhaustively addressed by Congress through the creation of a highly articulated administrative process. That process plainly governed the legitimacy of the discharges at issue in *City of Milwaukee*, and the City had in fact obtained discharge emission permits in accordance with it. 451 U.S. at 323-324. Permitting the development of a body of federal common law to govern the City's discharges would have simply amounted to extra-statutory judicial review of the federal and state administrative processes. *Id.* at 324. Such judicial review would have conflicted with the specific standards governing discharges of pollutants that Congress and the agencies to which it delegated power had developed. *Id.* at 324-325. It also would have conflicted with orderly judicial review of the agencies' actions through procedures established in accordance with federal and state law. Insofar as state common law continued to apply to discharges of pollutants, it was because Congress expressly provided that state law—including state common law—could impose *more stringent standards* than those provided for by the 1972 Amendments. See *id.* at 327 (discussing Section 510 of the statute, 33 U.S.C. 1370). Finally, the Court relied in part on the fact that federal common law would be particularly inappropriate because of the difficulty of applying the "ad hoc" approach of federal common law in an area of such great scientific and technical complexity. 451 U.S. at 325.

4. Petitioner essentially proposes three distinct ways in which FIRREA supposedly has covered the field at issue in this case so as to preclude the normal application of federal common law.

a. First, petitioner asserts (Pet. Br. 19-20) that a congressional intent to preempt federal common law

can be derived from the provision of FIRREA providing that the FDIC as receiver "succeed[s] to * * * all rights, titles, powers, and privileges of the insured depository institution." 12 U.S.C. 1821(d)(2)(A)(i) (Supp. IV 1922).[24] That provision is plainly intended to grant the FDIC certain rights as receiver; it does not purport, nor can it sensibly be read, to limit the FDIC's rights in any way. Indeed, later in the same section, Congress made quite clear that Section 1821(d)(2)(A) does not limit the FDIC's authority in this way or suggest that the FDIC has *only* the specific rights specified in that section by providing that that FDIC "may, as conservator or receiver * * * exercise all powers and authorities specifically granted to conservators or receivers * * * under this chapter *and such incidental powers as shall be* necessary to carry out such powers." 12 U.S.C. 1821(d)(2)(J) (Supp. IV 1992) (emphasis added). See also 12 U.S.C. 1821(d)(1) (Supp. IV 1992) (providing that FDIC "may prescribe such regulations as [it] determines to be appropriate regarding the conduct of conservatorships or receiverships"). As the *D'Oench, Duhme* doctrine establishes, receivers in some circumstances are not subject to defenses that might be available against the corporation to whose assets they succeed.[25] Congress did not intend to overrule that principle when it enacted FIRREA.

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[24] In one of its two alternative holdings, the Ninth Circuit held in this case that Sahni's and Day's wrongdoing could not be imputed to ADSB. See Pet. App. 10a-13a. That holding is sufficient to resolve this case, even if Section 1821(d)(2)(A)(i) could be read, as petitioner argues, strictly to limit the FDIC's rights as receiver to the precise rights that could have been exercised by the management of the insured financial institution itself.

[25] Cf. *Texas & Pacific Ry.* v. *Pottorff*, 291 U.S. 245, 260-261 (1934) ("even if the bank would have been estopped from asserting lack of power, its receiver would be free to challenge the validity of the pledge").

b. Second, petitioner argues (Pet. Br. 21-22) that FIRREA covers the field of defenses applicable to the FDIC as receiver. In that connection, petitioner cites a variety of provisions granting the FDIC certain powers and specifying certain rules that are to be applicable to suits brought by the FDIC.

For example, one of the provisions cited, 12 U.S.C 1821(e) (Supp. IV 1992), grants the FDIC as receiver the authority to repudiate contracts, 12 U.S.C. 1821(e)(1)-(2) (Supp. IV 1992), provides detailed instructions concerning the exercise of and consequences of such a repudiation, 12 U.S.C. 1821(e)(4)-(11) (Supp. IV 1992), and provides for claims and damages when that authority is exercised, 12 U.S.C. 1821(e)(3) (Supp. IV 1992). Section 1821(e), however, clearly does not mean generally to govern the assertion of equitable defenses against FDIC; its specific purpose is to codify what had previously been a federal common law doctrine concerning only the FDIC's power as receiver to repudiate contracts.[26]

Another provision on which petitioner relies provides for a statute of limitations applicable to actions brought by FDIC as receiver. See 12 U.S.C. 1821(d)(14) (Supp. IV 1992). That provision was plainly intended to supplant shorter state statutes of limitations, not fed-

[26] Although the authority of FSLIC as receiver to repudiate contracts was codified at 12 C.F.R. 569a.6(c)(3) (1982) and 12 C.F.R. 549.3(a) (1982), the FDIC had no parallel regulation. The courts had, however, recognized that, as receiver, FDIC necessarily had that authority. See, *e.g.*, *FDIC* v. *Grella*, 553 F.2d 258, 262-263 (2d Cir. 1977); *Argonaut Sav. & Loan Ass'n* v. *FDIC*, 392 F.2d 195, 197 (9th Cir.), cert. denied, 393 U.S. 839 (1968). Since FIRREA, the FDIC's powers to repudiate contracts are codified at 12 U.S.C. 1821(e) (Supp. IV 1992), and the Resolution Trust Corporation's similar powers are codified at 12 U.S.C. 1441a(b)(4)(A) (Supp. IV 1992). As the Committee Report on those provisions stated, they were intended to "incorporate[] rights and principles established at common law or in bankruptcy." S. Rep. No. 19, 101st Cong., 1st Sess. 314 (1989).

eral common law generally. See, *e.g.*, *FDIC* v. *New Hampshire Ins. Co.*, 953 F.2d 478, 486-488 (9th Cir. 1992); *FDIC* v. *McSweeney*, 976 F.2d 532, 534-536 (9th Cir. 1992), cert. denied, 113 S. Ct. 2440 (1993). In any event, Section 1821(d)(14) certainly does not govern the equitable defenses that may be asserted against the FDIC. Nor is there any basis for the proposition that its enactment reflected a general intent to limit the scope of federal common law, while leaving state common law intact, as petitioner argues.

One provision cited by petitioner, 12 U.S.C. 1823(e) (Supp. IV 1992), does directly govern an equitable defense that may be asserted against the FDIC. That provision is the one at issue in *Langley*, which renders certain unwritten and unrecorded side agreements unenforceable against the FDIC in an action on a note.[27] FIRREA slightly altered the wording of that provision, which was originally enacted in 1950. See Federal Deposit Insurance Act of 1950, ch. 967, § 2[13] [e], 64 Stat. 889. As explained above, see note 22, *supra*, although the provision does overlap the *D'Oench Duhme* doctrine substantially, the courts of appeals in the years since 1950 have recognized that it supplements, rather than supplants, the common law doctrine. As such, it could not possibly be read to have supplanted the entire field of federal common law regarding the defenses that may be asserted in suits brought by the FDIC as receiver.

c. Finally, petitioner cites two provisions of FIRREA that address malfeasance by financial institution insiders and professionals employed by such institutions. One of them, 12 U.S.C. 1821(k) (Supp. IV 1992), provides that the FDIC may bring suit against directors or officers of insured depository institutions for damages caused by

[27] Another provision cited by petitioner (Pet. Br. 22) 12 U.S.C. 1821(d)(9) (Supp. IV 1992), applies the rule of Section 1823(e) to claims *against* FDIC.

their "gross negligence." Outside attorneys and accountants are not governed by that provision, and it would be odd to read it to have any effect on malpractice actions against them. In any event, however, Congress made quite clear the extent to which it intended Section 1821 (k) to preempt other sources of law by providing that "[n]othing in this [Section] shall impair or affect any right of the [FDIC] under other applicable law." 12 U.S.C. 1821(k) (Supp. IV 1992). There is no reason not to take that language literally.[28]

FIRREA also modified the pre-existing authority of FDIC as regulator to impose administrative penalties on individuals affiliated with insured financial institutions. Prior to the enactment of FIRREA, both the FDIC and FSLIC could impose administrative sanctions for violation of the agency's orders against directors and officers of regulated institutions, as well as others who "participat[ed] in the conduct of the affairs" of such institutions. 12 U.S.C. 1818(i)(2)(i) (1988).[29] Cf. *Reves*

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[28] The purpose of Section 1821(k) was to preempt state laws that purport to insulate officers or directors of financial institutions from liability. See *FDIC* v. *McSweeney*, 976 F.2d at 539-540; *FDIC* v. *Canfield*, 967 F.2d 443, 448 n.6 (10th Cir.) (en banc), cert. dismissed, 113 S. Ct. 516 (1992). As the Senate Report explained, Section 1821(k) "does not prevent the FDIC from pursuing claims under State law *or under other applicable Federal law*, if such law permits the officers or directors of a financial institution to be sued * * * for violating a lower standard of care, such as simple negligence." S. Rep. No. 19, *supra*, at 318 (emphasis added).

[29] 12 U.S.C. 1818(i)(2)(i) (1988) provided that "[a]ny insured bank" or "any officer, director, employee, agent, or other person participating in the conduct of the affairs of such a bank who violates" a final order of the "appropriate Federal banking agency" may be fined up to $1,000 per day. That provision thus applied to attorneys only insofar as they "participat[ed] in the conduct of the affairs" of the institution. The term "appropriate Federal banking agency" was defined to include, *inter alia*, the FDIC and

v. *Ernst & Young*, 113 S. Ct. 1163 (1993). FIRREA augmented that procedure by dramatically increasing the maximum penalty[30] and by enlarging the types of conduct that would subject a party to an administrative penalty to include, in specified circumstances, "recklessly engag[ing] in an unsafe or unsound practice," 12 U.S.C. 1818(i)(2)(B)(i)(II) (Supp. IV 1992), "breach[ing] any fiduciary duty," 12 U.S.C. 1818(i)(2)(B)(i)(III) Supp. IV 1992), and "knowingly or recklessly caus[ing] a substantial loss" to the institution, 12 U.S.C. 1818 (i)(2)(C)(ii) (Supp IV 1992). FIRREA also widened the category of attorneys and accountants who could be subject to the administrative penalty; that group was enlarged to include any attorney or accountant "who knowingly or recklessly" committed one of the administrative infractions mentioned above. 12 U.S.C. 1813(u) (4) (Supp. IV 1992).[31]

FIRREA's modification of the FDIC administrative penalty provision in no way suggests that Congress intended to preempt all federal common law—but not state common law—principles that might govern attorney malpractice suits, as petitioner suggests. On the contrary, Congress's strengthening of the administrative penalty provision has nothing to do with *limiting* the scope or nature of negligence actions that may be brought against professionals employed by insured institutions, or with the rules of law that apply to such actions.

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the Federal Home Loan Bank Board, which regulated thrift institutions. 12 U.S.C. 1813(q) (1988).

[30] Prior to FIRREA, the maximum penalty was $1,000 per day. 12 U.S.C. 1818(i)(2)(i) (1988). FIRREA established a graduated schedule with penalties ranging from a maximum of $5,000 per day to a maximum of $1,000,000 per day, depending on the nature of the violation. See 12 U.S.C. 1818(i)(2) (Supp. IV 1992).

[31] Section 1813(u) defines the term "institution-affiliated party." In turn, 12 U.S.C. 1818(i)(2) (Supp. IV 1992) grants the FDIC authority to impose penalties on any "institution-affiliated party."

An administrative penalty and a negligence action for damages are not plausible substitutes for one another, such that Congress could be understood to have eliminated the latter when it strengthened the former. Administrative penalty proceedings serve deterrent purposes, while the primary function of a tort suit is to compensate the victim of the tort. Administrative penalty proceedings may be instituted against those associated with institutions regardless of whether the institutions are solvent or in receivership, while negligence actions brought by the FDIC as receiver are by definition brought only against individuals who have harmed an insolvent institution. In addition, administrative penalties are to be assessed in proportion to the seriousness of the misconduct, while in negligence actions, damages are measure by the loss suffered by the victim. Finally, administrative penalties must by statute be deposited in the federal treasury, 12 U.S.C. 1818(i)(2)(J) (Supp. IV 1992), while the proceeds of a malpractice action go to the insurance fund or the receivership estate to repay the fund or the estate for the harm done by the negligence. In light of these striking differences between the two remedies it would be illogical to conclude that Congress implicitly intended to restrict suits for professional malpractice by strengthening the administrative penalties available against attorneys and accountants for their misconduct.

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At bottom, petitioner's argument is that, because Congress enacted legislation governing the legal relations of the FDIC in certain specific areas that were formerly governed by federal common law or state law, Congress's silence on other matters should somehow be read to have entirely supplanted the field of federal common law governing the FDIC, while somehow leaving state common law intact. That is a highly unlikely conclusion, especially because two of this Court's earliest and most prominent federal common law decisions after *Erie R.R.* v. *Tompkins*, 304 U.S. 64 (1938), concerned the rights and responsibilities of the FDIC as receiver. See *Deitrick* v. *Greaney*, 309 U.S. 190 (1940); *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942). FIRREA itself was enacted to "*strengthen* the enforcement powers of Federal regulators of depository institutions," § 101(9), 103 Stat. 187 (codified at 12 U.S.C. 1811 note (Supp. IV 1992) (emphasis added)) not to limit them. The federal common law rule that we advocate in this case is fully consistent with the leading cases and with the prevalent state common law rules governing the subject. It is the only rule that adequately takes into account the unique federal interests that come into play when the FDIC becomes receiver of an insured depository institution. The Ninth Circuit's decision should therefore be affirmed.

CONCLUSION

The decision of the Ninth Circuit should be affirmed.

Respectfully submitted.

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APPENDIX

12 U.S.C. 1813

* * * * *

(q) Appropriate Federal banking agency

The term "appropriate Federal banking agency" means—

(1) the Comptroller of the Currency, in the case of any national banking association, any District bank, or any Federal branch or agency of a foreign bank;

(2) the Board of Governors of the Federal Reserve System, in the case of—

(A) any State member insured bank (except a District bank),

(B) any branch or agency of a foreign bank with respect to any provision of the Federal Reserve Act [12 U.S.C.A. § 221 et seq.] which is made applicable under the International Banking Act of 1978 [12 U.S.C.A. § 3101 et seq.],

(C) any foreign bank which does not operate an insured branch,

(D) any agency or commercial lending company other than a Federal agency,

(E) supervisory or regulatory proceedings arising from the authority given to the Board of Governors under section 7(c)(1) of the International Banking Act of 1978 [12 U.S.C.A. § 3105(b)(1)], including such proceedings under the Depository Institutions Supervisory Act, and

(F) any bank holding company and any subsidiary of a bank holding company (other than a bank);

(3) the Federal Deposit Insurance Corporation in the case of a State nonmember insured bank (except a District bank), or a foreign bank having an insured branch; and

(4) the Director of the Office of Thrift Supervision in the case of any savings association or any savings association or any savings and loan holding company.

Under the rule set forth in this subsection, more than one agency may be an appropriate Federal banking agency with respect to any given institution.

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(u) INSTITUTION AFFILIATED PARTY.—The term "institution-affiliated party" means—

(1) any director, officer, employee, or controlling stockholder (other than a bank holding company) of, or agent for, an insured depository institution;

(2) any other person who has filed or is required to file a change-in-control notice with the appropriate Federal banking agency under section 1817(j) of this title;

(3) any shareholder (other than a bank holding company) consultant, joint venture partner, and any other person as determined by the appropriate Federal banking agency (by regulation or case-by-case) who participates in the conduct of the affairs of an insured depository institution; and

(4) any independent contractor (including any attorney, appraiser, or accountant) who knowingly or recklessly participates in—

(A) any violation of any law or regulation;
(B) any breach of fiduciary duty; or
(C) any unsafe or unsound practice,

which caused or is likely to cause more than a minimal financial loss to, or a significant adverse effect on, the insured depository institution.

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12 U.S.C. 1818

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(i) Jurisdiction and enforcement; penalty

(1) The appropriate Federal banking agency may in its discretion apply to the United States district court, or the United States court of any territory, within the jurisdiction of which the home office of the depository institution is located, for the enforcement of any effective and outstanding notice or order issued under this section or under section 1831*o* or 1831p-1 of this title, and such courts shall have jurisdiction and power to order and require compliance herewith; but except as otherwise provided in this section or under section 1831*o* or 1831p-1 of this title no court shall have jurisdiction to affect by injunction or otherwise the issuance or enforcement of any notice or order under any such section, or to review, modify, suspend, terminate, or set aside any such notice or order.

(2) CIVIL MONEY PENALTY.—

(A) FIRST TIER.—Any insured depository institution which, and any institution-affiliated party who—

(i) violates any law or regulation;

(ii) violates any final order or temporary order issued pursuant to subsection (b), (c), (e), (g), or (s) of this section or any final order under section 1831*o* or 1831p-1 of this title;

(iii) violates any condition imposed in writing by the appropriate Federal banking agency

in connection with the grant of any application or other request by such depository instituiton; or

(iv) violates any written agreement between such depository institution and such agency,

shall forfeit and pay a civil penalty of not more than $5,000 for each day during which such violation continues.

(B) SECOND TIER.—Notwithstanding subparagraph (A), any insured depository institution which, and any institution-affiliated party who—

(i)(I) commits any violation described in any clause of subparagraph (A);

(II) recklessly engages in an unsafe or unsound practice in conducting the affairs of such insured depository institution; or

(III) breaches any fiduciary duty;

(ii) which violation, practice, or breach—

(I) is part of a pattern of misconduct;

(II) causes or is likely to cause more than a minimal loss to such depository institution; or

(III) results in pecuniary gain or other benefit to such party,

shall forfeit and pay a civil penalty of not more than $25,000 for each day during which such violation, practice, or breach continues.

(C) THIRD TIER.—Notwithstanding subpragraphs (A) and (B), any insured depository institution which, and any institution-affiliated party who—

(i) knowingly—

(I) commits any violation described in any clause of subparagraph (A);

(II) engages in any unsafe or unsound practice in conducting the affairs of such depository institution; or

(III) breaches any fiduciary duty; and

(ii) knowingly or recklessly causes a substantial loss to such depository institution or a substantial pecuniary gain or other benefit to such party by reason of such violation, practice, or breach,

shall forfeit and pay a civil penalty in an amount not to exceed the applicable maximum amount determined under subparagraph (D) for each day during which such violation, practice, or breach continues.

(D) MAXIMUM AMOUNTS OF PENALTIES FOR ANY VIOLATION DESCRIBED IN SUBPARAGRAPH (c).—The maximum daily amount of any civil penalty which may be assessed pursuant to subparagraph (C) for any violation, practice, or breach described in such subparagraph is—

(i) in the case of any person other than an insured depository institution, an amount to not exceed $1,000,000; and

(ii) in the case of any insured depository institution, an amount not to exceed the lesser of—

(I) $1,000,000; or

(II) 1 percent of the total assets of such institution.

(E) ASSESSMENT.—

(i) WRITTEN NOTICE.—Any penalty imposed under subparagraph (A), (B), or (C) may be assessed and collected by the appropriate Federal banking agency by written notice.

(ii) FINALITY OF ASSESSMENT.—If, with respect to any assessment under clause (i), a hearing is not requested pursuant to subparagraph (H) within the period of time allowed under such subparagraph, the assessment shall constitute a final and unappealable order.

(F) AUTHORITY TO MODIFY OR REMIT PENALTY.—Any appropriate Federal banking agency may compromise, modify, or remit any penalty which such agency may assess or had already assessed under subparagraph (A), (B), or (C).

(G) MITIGATING FACTORS.—In determining the amount of any penalty imposed under subparagraph (A), (B), or (C), the appropriate agency shall take into account the appropriateness of the penalty with respect to—

(i) the size of financial resources and good faith of the insured depository institution or other person charged;

(ii) the gravity of the violation;

(iii) the history of previous violations; and

(iv) such other matters as justice may require.

(H) HEARING.—The insured depository institution or other person against whom any penalty is assessed under this paragraph shall be afforded an agency hearing if such institution or person submits a request for such hearing within 20 days after the issuance of the notice of assessment.

(I) COLLECTION.—

(i) REFERRAL.—If any insured depository institution or other person fails to pay an assessment after any penalty assessed under this paragraph has become final, the agency that imposed

the penalty shall recover the amount assessed by action in the appropriate United States district court.

(ii) APPROPRIATENESS OF PENALTY NOT REVIEWABLE.—In any civil action under clause (i), the validity and appropriateness of the penalty shall not be subject to review.

(J) DISBURSEMENT.—All penalties collected under authority of this paragraph shall be deposited into the Treasury.

(K) REGULATIONS.—Each appropriate Federal banking agency shall prescribe regulations establishing such procedures as may be necessary to carry out this paragraph.

(3) NOTICE UNDER THIS SECTION AFTER SEPARATION FROM SERVICE.—The resignation, termination of employment or participation, or separation of a institution-affiliated party (including a separation caused by the closing of an insured depository institution shall not affect the jurisdiction and authority of the appropriate Federal banking agency to issue any notice and proceed under this section against any such party, if such notice is served before the end of the 6-year period beginning on the date such party ceased to be such a party with respect to such depository institution (whether such date occurs before, on, or after August 9, 1989).

(4) PREJUDGEMENT ATTACHMENT.—

(A) IN GENERAL.—In any action brought by an appropriate Federal banking agency (excluding the Corporation when acting in a manner described in section 1821(d)(18) of this title) pursuant to this section, or in actions brought in aid of, or to enforce an order in, any administrative or other civil action for money damages, restitution, or civil money penalties brought by such agency, the court may, upon

application of the agency, issue a restraining order that—

(i) prohibits any person subject to the proceeding from withdrawing, transferring, removing, dissipating, or disposing of any funds, assets or other property; and

(ii) appoints a temporary receiver to administer the restraining order.

(B) STANDARD.—A permanent or temporary injunction or restraining order shall be granted without bond upon a prima facie showing that money damages, restitution, or civil money penalties, as sought by such agency, is appropriate.

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12 U.S.C. 1821

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(d) Powers and duties of Corporation as conservator or receiver

(1) Rulemaking authority of Corporation

The Corporation may prescribe such regulations as the Corporation determines to be appropriate regarding the conduct of conservatorships or receiverships.

(2) General powers

(A) Successor to institution

The Corporation shall, as conservator or receiver, and by operation of law, succeed to—

(i) all rights, titles, powers, and privileges of the insured depository institution, and of any stockholder, member, accountholder, depositor, officer, or director of such institution with respect to the insti-

tution and the assets of the institution; and

(ii) title to the books, records, and assets of any previous conservator or other legal custodian of such institution.

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12 U.S.C. 1821(d)(2):

(J) Incidental powers

The Corporation may, as conservator or receiver—

(i) exercise all powers and authorities specifically granted to conservators or receivers, respectively, under this chapter and such incidental powers as shall be necessary to carry out such powers; and

(ii) take any action authorized by this chapter,

which the Corporation determines is in the best interests of the depository institution, its depositors, or the Corporation.

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12 U.S.C. 1821(d):

(9) Agreement as basis of claim

(A) Requirements

Except as provided in subparagraph (B), any agreement which does not meet the requirements set forth in section 1823(e) of this title shall not form the basis of, or substantially compromise, a claim against the receiver or the Corporation.

(B) Exception to contemporaneous execution requirement

Notwithstanding section 1823(e)(2) of this title, any agreement relating to an extension of credit between a Federal home loan bank or Federal Reserve bank and any insured depository institution which was executed before the extension of credit by such bank to such institution shall be treated as having been executed contemporaneously with such extension of credit for purposes of subparagraph (A).

* * * * *

(14) Statute of limitations for actions brought by conservator or receiver

(A) In general

Notwithstanding any provision of any contract, the applicable statute of limitations with regard to any action brought by the Corporation as conservator or receiver shall be—

(i) in the case of any contract claim, the longer of—

(I) the 6-year period beginning on the date the claim accrues; or

(II) the period applicable under State law; and

(ii) in the case of any tort claim, the longer of—

(I) the 3 year period beginning on the date the claim accrues; or

(II) the period applicable under State law.

(B) Determination of the date on which a claim accrues

For purposes of subparagraph (A), the date on which the statute of limitation begins to run

on any claim described in such subparagraph shall be the later of—

(i) the date of the appointment of the Corporation as conservator or receiver; or

(ii) the date on which the cause of action accrues.

* * * * *

(e) Provisions relating to contracts entered into before appointment of conservator or receiver

(1) Authority to repudiate contracts

In addition to any other rights a conservator or receiver may have, the conservator or receiver for any insured depository institution may disaffirm or repudiate any contract or lease—

(A) to which such institution is a party;

(B) the performance of which the conservator or receiver, in the conservator's or receiver's discretion, determines to be burdensome; and

(C) the disaffirmance or repudiation of which the conservator or receiver determines, in the conservator's or receiver's discretion, will promote the orderly administration of the institution's affairs.

(2) Timing of repudiation

The conservator or receiver appointed for any insured depository institution in accordance with subsection (c) of this section shall determine whether or not to exercise the rights of repudiation under this subsection within a reasonable period following such appointment.

(3) Claims for damages for repudiation

(A) In general

Except as otherwise provided in subparagraph (C) and paragraphs (4), (5), and (6), the liability of the conservator or receiver for the disaffirmance or repudiation of any contract pursuant to paragraph (1) shall be—

(i) limited to actual direct compensatory damages; and

(ii) determined as of—

(I) the date of the appointment of the conservator or receiver; or

(II) in the case of any contract or agreement referred to in paragraph (8), the date of the disaffirmance or repudiation of such contract or agreement.

(B) No liability for other damages

For purposes of subparagraph (A), the term "actual direct compensatory damages" does not include—

(i) punitive or exemplary damages;

(ii) damages for lost profits or opportunity; or

(iii) damages for pain and suffering.

(C) Measure of damages for repudiation of financial contracts

In the case of any qualified financial contract or agreement to which paragraph (8) applies, compensatory damages shall be—

(i) deemed to include normal and reasonable costs of cover or other reasonable measures of damages utilized in the industries for such contract and agreement claims; and

(ii) paid in accordance with this subsection and subsection (k) of this section

except as otherwise specifically provided in this section.

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12 U.S.C. 1821:

(k) Liability of directors and officers

A director or officer of an insured depository institution may be held personally liable for monetary damages in any civil action by, on behalf of, or at the request or direction of the Corporation, which action is prosecuted wholly or partially for the benefit of the Corporation—

(1) acting as conservator or receiver of such institution,

(2) acting based upon a suit, claim, or cause of action purchased from, assigned by, or otherwise conveyed by such receiver or conservator, or

(3) acting based upon a suit, claim, or cause of action purchased from, assigned by, or otherwise conveyed in whole or in part by an insured depository institution or its affiliate in connection with assistance provided under section 1823 of this title,

for gross negligence, including any similar conduct or conduct that demonstrates a greater disregard of a duty of care (than gross negligence) including intentional tortious conduct, as such terms are defined and determined under applicable State law. Nothing in this paragraph shall impair or affect any right of the Corporation under other applicable law.

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12 U.S.C. 1823

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(e) Agreements against interests of Corporation

No agreement which tends to diminish or defeat the interest of the Corporation in any asset acquired by it

under this section or section 1821 of this title, either as security for a loan or by purchase or as receiver of any insured depository institution, shall be valid against the Corporation unless such agreement—

(1) is in writing,

(2) was executed by the depository institution and any person claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the depository institution,

(3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and

(4) has been, continuously, from the time of its execution, an official record of the depository institution.

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